Supreme Court, U.S.
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No. 93-578

IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1993

SNAP-ON TOOLS CORPORATION, JAMES GOMENDI and STEVE GULLEDGE

Petitioners,

v.

WILLIAM C. VETTER and ELAINE LaPOINTE-VETTER,

Respondents.

Petition For A Writ of Certiorari To The Montana District Court For The Fourth Judicial District, Missoula County, Montana

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RESPONDENTS' BRIEF IN OPPOSITION

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QUESTIONS PRESENTED FOR REVIEW

1. Does diversity of citizenship jurisdiction exist over a petition to compel arbitration where one of the parties seeking to compel arbitration is non-diverse to the opposing party, yet is not formally joined as a party in order to create federal subject matter jurisdiction?

2. Should a federal court abstain from exercising jurisdiction over arbitration issues, which a state court is in the process of adjudicating, where the federal court does not have subject matter jurisdiction to resolve the entire arbitration controversy?

3. Does the "protect or effectuate its judgments" exception to the anti-injunction statute [28 U.S.C. § 2283] permit a federal court to enjoin a parallel state court proceeding involving the identical issues, where the state court first exercised jurisdiction over those issues?

4. Is the Montana Uniform Arbitration Act's requirement that all contracts with an arbitration clause contain a conspicuous warning notice on the front page pre-empted by the Federal Arbitration Act, despite this Court's approval of state arbitration law procedural provisions in Volt Information Sciences, Inc. v. Board of Trustees, 489 U.S. 468 (1989)?

5. Are general state law prohibitions against forum selection clauses, and clauses limiting the time period for bringing legal action, pre-empted by the Federal Arbitration Act when those clauses are contained in an arbitration contract?

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SUMMARY OF ARGUMENT

The State Court Order which Petitioners request this Court to review was not final and is now moot. The stay pending arbitration requested by Petitioners has now been granted. The mandatory or discretionary nature of 9 U.S.C. § 3 is not an issue in this case.

This case does, however, present important questions concerning the authority of federal courts to interfere with an ongoing state court disposition of arbitration issues. This case also raises important issues regarding the ability of the states to insure voluntary, knowing, and even-handed agreements to arbitrate, an objective which is entirely consistent with the Federal Arbitration Act.

The Petition should be denied, or if granted, the the entire arbitration controversy, as framed in two parallel state and federal actions, should be reviewed.

CLARIFICATION OF FACTS

Petitioners Snap-On Tools Corporation ("Snap-On"), James Gomendi ("Gomendi"), and Steve Gulledge (collectively "Petitioners") have framed the issue on the instant Petition for Writ of Certiorari ("Petition") as turning "entirely on whether 9 U.S.C. § 3 is applicable to state-court proceedings." Petition, pages 5-6. Petitioners implicitly argue that the Montana District Court for the Fourth Judicial District, Missoula County, Montana ("State Court") finally resolved all arbitration issues against Petitioners by ruling that 9 U.S.C. § 3 is discretionary, and not mandatory.

Petitioners have mischaracterized the proceedings below. 9 U.S.C. § 3 has no bearing on this case. What this case does involve, however, is the role of federal courts in resolving arbitration issues pending before state courts, and the power of the federal courts to enjoin a

state court from continuing to adjudicate arbitration issues over which the latter first exercised jurisdiction. This case invokes state/federal jurisdictional principles lying at the very heart of our federalist system.

A brief review of the procedural background of this dispute will assist in understanding the true nature of the issues presented by this case.

Respondent William C. Vetter ("William") and his wife, Elaine LaPointe-Vetter ("Elaine") [collectively the "Vetters"] filed the subject action[1] in the State Court on

[1]The State Court action, bearing Cause No. 77498 in the files of the Montana State Court, shall be referred to as the "State Action." The parties in the State Action are the Vetters, as plaintiffs, and all three Petitioners, as defendants. Petitioners Gomendi and Gulledge, who are employees of Petitioner Snap-On, were the principal actors causing the damage to the Vetters sought in the State Action. After being served in the State Action, Snap-On alone filed a companion federal court suit, bearing Cause No. CV 93-34-M-CCL (the "Federal Action") in the files of the United States District Court for the District of Montana, Missoula Division (the "Federal Court"), against William alone. Gomendi and Gulledge were not named as parties to the Federal Action because that would destroy the diversity jurisdiction of the Federal Court. However, Snap-On sought relief on behalf of Gomendi and Gulledge in the Federal Action. See discussion at pages 3-7, infra.

February 24, 1993, alleging various common law tort claims against Petitioners. Essentially, the Vetters alleged, first, that Petitioners had fraudulently induced them to invest their life savings in a failing Snap-On dealership, and second, that Petitioners had interfered with the Vetters' business relationships with actual and potential customers. The Vetters asserted that, as a result of Petitioners' activities, the dealership failed, the Vetters lost all of their life savings, and they incurred additional debts which put them on the verge of bankruptcy.

Petitioners responded to the Vetters' allegations on two fronts. First, Petitioners filed a motion to stay, pursuant to 9 U.S.C. § 3, in the State Action, seeking a stay of all claims[2] pending arbitration of William's claims against all three Petitioners. Second, Snap-On alone filed the Federal Action, seeking an order, pursuant to 9

[2]Petitioners sought a stay against Elaine's claims even though she signed no arbitration agreement.

U.S.C. § 4, compelling William to arbitrate his claims against all three Petitioners. Importantly, Petitioners did not request the State Court for an order compelling William to arbitrate his claims, even though Montana law[3] clearly permits a Montana state court to order such relief. The race to judgment on the competing arbitration motions in State Court and Federal Court then began.[4]

[3]Montana has adopted the Uniform Arbitration Act. Montana Code Annotated § 27-5-115(1) specifically allows a Montana state court to compel a party to arbitrate its claims if the court finds a valid arbitration agreement to exist. Petitioners initially argued that they were relying solely on the Federal Arbitration Act and that 9 U.S.C. § 4 did not apply in state courts. Interestingly, in October, 1993, after the Federal Court ruled in Snap-On's favor, Petitioners went back to State Court and sought an order compelling William to arbitrate his claims against Gomendi and Gulledge based upon 9 U.S.C. § 4. Thus, Petitioners' initial position that 9 U.S.C. § 4 only applied in federal courts was obviously asserted solely to enable Petitioners to forum shop for a federal judge who might be more favorable to their positions on arbitration, rather than due to any jurisdictional concerns.

[4]It is important to note that the multiplicitous proceedings which have occurred in this dispute to date have all focused upon the validity of the subject arbitration clause. Notwithstanding their touting the speed, efficiency and economy of arbitration, Petitioners have spread the instant arbitration controversy over the files of five adjudicatory bodies. In addition to filing the motion to stay pending arbitration in the State Action, Petitioners filed the Federal Action seeking an order

William moved to dismiss the Federal Action on the ground that the Federal Court lacked subject matter jurisdiction of the arbitration controversy. William argued that Gomendi, a Montana resident, was an indispensable party to the Federal Action because Snap-On sought enforcement of the subject arbitration clause[5] on

compelling arbitration. Petitioners then both sought a writ of supervisory control from and appealed to the Montana Supreme Court, and ultimately filed the Petition with this Court, seeking to overturn the State Court order denying a stay pending arbitration. Finally, Petitioners instituted arbitration proceedings with the American Arbitration Association, seeking an adjudication that William's claims in the State Action have no merit. William has not participated in the AAA arbitration because he can not afford to do so and his participation could waive his argument that the subject arbitration clause is invalid. Throughout all of these proceedings, the Vetters have consistently maintained that the State Court is the only body with jurisdiction to resolve all arbitration issues between all interested parties.

[5]The subject arbitration clause appears as paragraph 11 of the Dealership Agreement between William and Snap-On. A portion of that clause has been quoted at pages 2-3 of the Petition. The entire clause shall hereafter be referred to as the "Arbitration Clause". As discussed at p. 19, infra, the Arbitration Clause contains several one-sided provisions which favor Petitioners only. For example, the Arbitration Clause requires William to litigate all of his disputes in the State of Wisconsin, Snap-On's home base, and shortens the statute of limitations on all claims to one year. Montana law prohibits such provisions in all contracts, whether they concern litigation, arbitration, mediation, or any other means of dispute resolution.

Gomendi's behalf. Because the Federal Arbitration Act does not create an independent basis of federal jurisdiction [see Moses H. Cone Memorial Hospital v. Mercury Construction Corporation, 460 U.S. 1, 25, fn. 32 (1983)], and diversity of citizenship jurisdiction was lacking over an indispensable party to the arbitration controversy, William argued that the Federal Action should be dismissed for lack of subject matter jurisdiction.

Alternatively, William argued that the Federal Court should abstain from exercising jurisdiction because the State Court had already commenced exercising its unquestioned jurisdiction to resolve all arbitration issues. Federal court intervention in the process would inevitably result in piecemeal resolution of arbitration issues. Not only was the Federal Court unable to adjudicate the validity of the Arbitration Clause insofar as it concerned the claims against Gomendi, but the Federal Court did not have jurisdiction to confirm any arbitration award

between the parties [see General Atomic Company v. United Nuclear Corporation, 655 F.2d 968 (9th Cir. 1981)].

William's motion to dismiss the Federal Action was pending until September 27, 1993, at which time the Federal Court denied the same.

In the meantime, proceedings were ongoing in the State Court to resolve the same arbitration issues. On May 27, 1993, the State Court temporarily denied[6] Petitioners' Motion to Stay the State Action pending arbitration, ruling that the parties should present all of their arbitration arguments to it in subsequent proceedings. After unsuccessfully seeking review of that interlocutory order in the Montana Supreme Court, Petitioners ran back to the Federal Court and filed an

[6]This is the order of which Petitioners seek review by this Court. As noted at pages 12-13, infra, this order did not finally adjudicate any arbitration issues, but was designed solely to force all parties to present to the State Court all of their positions on the enforceability of the Arbitration Clause.

application for an injunction against further prosecution of the State Action. Nonetheless, William heeded the State Court's instructions and filed a motion in the State Action requesting resolution of all arbitration issues. At the same time William opposed Snap-On's application to the Federal Court for an injunction against the State Action.

Ultimately, Snap-On won the race to judgment. On October 8, 1993, the Federal Court granted Snap-On's motion to compel William to arbitrate his claims, and enjoined further prosecution of the State Action by William. The Federal Court overruled, as a matter of law, all six of William's challenges to the validity of the Arbitration Clause.[7] The Federal Court denied William

[7]William argued that the Arbitration Clause was invalid because: (1) the contract did not contain the conspicuous warning notice mandated by Montana Code Annotated § 27-5-114(4); (2) it contained forum selection and limitation of action provisions which are prohibited by Montana law in any contract; (3) it lacked consideration and mutuality of remedy because it permitted Snap-On to seek judicial relief on its only meaningful

his right to a jury trial of the factual issues underlying those challenges [see 9 U.S.C. § 4; Par-Knit Mills, Inc. v. Stockbridge Fabrics Company, 636 F.2d 51, 54 (3rd Cir. 1980)][8] However, the Federal Court did not resolve any arbitration issues between William, Gomendi and Gulledge, nor any issues dealing with the stay of Elaine's claims pending arbitration of William's claims.[9]

claims, yet required William to arbitrate all of his claims against Snap-On; (4) it was voidable on the ground of constructive fraud under Montana law because Snap-On induced a false impression in William's mind as to the effect of the Arbitration Clause; (5) due to the oppressive and one-sided nature of this specific Arbitration Clause, it was "unconscionable" under Montana law, which applies this doctrine to all contracts; and (6) the language of the Arbitration Clause only required arbitration of disputes arising out of the Dealership Agreement, whereas William's claims related only to the dealings of the parties, and none of the parties relied upon any provision of the Dealership Agreement to prosecute or defend against William's claims.

[8]The Federal Court order is currently on appeal to the United States Court of Appeals for the Ninth Circuit. William filed his Notice of Appeal on October 29, 1993.

[9]It is undisputed that Elaine did not sign the Arbitration Clause. Nonetheless, Petitioners argued that the result of William's arbitration would collaterally estop Elaine. Elaine successfully argued to the State Court that she would not be bound by the results of William's arbitration because she possessed separate and independent claims against Petitioners.

A hearing was then held in the State Action on William's motion to adjudicate the same arbitration issues resolved by the Federal Court [namely, whether the Arbitration Clause was invalid and unenforceable], as well as those arbitration issues left unresolved by the Federal Court. Deciding that it was bound by the collateral estoppel effect of the Federal Court order, the State Court did not rule on the merits of William's challenges to the Arbitration Clause, and denied William's motion. The State Court also ruled that Elaine could continue to prosecute her claims against Petitioners as she would not be bound by the results of William's arbitration.

Thus, there are now orders from two courts of concurrent jurisdiction resolving arbitration issues emanating from the same lawsuit. Were it not for the deference shown by the State Court to the Federal Court order, a deference which the Federal Court refused to give to the earlier orders of the State Court, inevitably

this case would involve conflicting adjudications of the same arbitration issues. The net result of the proceedings below is that the Federal Court acted as an appellate tribunal over the State Court, a role which this Court has long disavowed for the federal judiciary [see Atlantic Coast Line Railroad Company v. Brotherhood of Locomotive Engineers, 398 U.S. 281, 295-96 (1970)].

Petitioners' request for this Court to review the May 27, 1993 State Court Order is thus misplaced. Not only did the State Court not finally adjudicate any arbitration issues by that Order, but all issues emanating from that Order are now moot. The intent of that Order was to hold that a viable dispute existed as to the validity of the Arbitration Clause, thus requiring all parties to present to the State Court all arguments concerning the enforceability of that clause.

In its response filed in the Montana Supreme Court regarding Petitioners' Application for a Writ of

Supervisory Control, the State Court clarified its May 27, 1993 Order as follows:

> "[T]he District Court found that there were potential issues with respect to the validity of the arbitration clause. Because Snap-On did not make a motion to compel arbitration in the District Court, the District Court did not make a finding as to the validity of the arbitration clause. It did, however, find that, based on the pleadings, claims have been stated by the Vetters that may not be subject to the arbitration clause. The District Court therefore denied Snap-On's motion to stay in order to give the Vetters an opportunity to argue in the District Court that the arbitration clause was invalid or inapplicable. The District Court did not find the arbitration clause invalid; it simply permitted the Vetters to argue in the District Court that it was invalid.
>
> "[T]he District Court's denial of Snap-On's motion for stay did not harm or prejudice Snap-On. The District Court did not make any final judgment and did not dispense with any claims. It simply allowed the Vetters' action to proceed to the next stage of litigation.
>
> * * *
>
> "The District Court's denial of Snap-On's motions has not in any way affected Snap-On's

> rights. Both the Vetters and Snap-On will have an opportunity to argue to the District Court that the Vetters' claims are subject to arbitration. Snap-On has not been deprived of its alleged right to arbitration; it has simply been required to make its arbitration argument in the District Court where the entire action began." [Emphasis added].

In essence, the State Court temporarily denied Petitioners' request for a stay pending arbitration. It then held that both Petitioners and the Vetters would have to present to it, in a subsequent proceeding, all of their arguments concerning the validity of the Arbitration Clause. Petitioners ultimately received the requested stay, albeit by improper resort to Federal Court.

The net result of all of these maneuverings, then, is that Snap-On bifurcated the arbitration dispute between two courts of concurrent jurisdiction in an effort to obtain a more favorable forum for resolution of its arguments concerning the validity of the Arbitration Clause. It then utilized the results of its forum shopping to collaterally estop William in the State Court, and thus deprive the

State Court of its unquestioned jurisdiction to resolve arbitration issues.

If such an effort is sanctioned, the federal courts will ultimately become the arbiters of every arbitration controversy emanating from state court cases in which there is any party of diverse citizenship. For that party could selectively sue in federal court a diverse party from the other side of the state court case, obtain a determination as to the validity of the arbitration agreement, and then run back to state court arguing that the state court was collaterally estopped from resolving the same arbitration issues. The potential conflicts between the state and federal courts in these circumstances abound. If this Court decides to exercise its discretionary jurisdiction to review the State Court Order, it should assume jurisdiction over the entire controversy, including all federal jurisdictional issues necessarily involved.

IMPORTANT QUESTIONS ARE PRESENTED BY THE ENTIRE CONTROVERSY WHICH SHOULD BE REVIEWED BY THIS COURT

If this Court decides to grant certiorari in this case, it should exercise jurisdiction over both pending actions, the State Action and the Federal Action. The Federal Action is currently on appeal to the Ninth Circuit Court of Appeals. The State Action is on hold, insofar as William's claims are concerned. Petitioners are attempting to adjudicate William's claims in the AAA arbitration, although William can not and will not participate in that arbitration. The State Action is moving forward to adjudicate the claims of Elaine, who signed no arbitration agreement.

Review by this Court of the entire controversy will resolve important questions concerning the interaction of the federal and state courts in resolving arbitration issues emanating from a proceeding in one of those courts. For

example:

1. Does a federal court possess diversity of citizenship jurisdiction over a petition to compel arbitration where one of the parties seeking to compel arbitration is non-diverse to the opposing party, yet is not formally joined as a party petitioner in order to create federal subject matter jurisdiction? An unbroken line of precedent [E.g., Wilson v. Oswego Township, 151 U.S. 56 (1894)] holds that the non-diverse citizenship of absent indispensable[10] parties destroys federal subject matter jurisdiction. The Federal Court Order ignores these established limitations on federal court jurisdiction.

2. Do the abstention principles relevant to

[10]The "indispensability" of Gomendi to the Federal Action is best demonstrated by the fact that, after obtaining the Federal Court Order compelling William to arbitrate his claims against Snap-On, Petitioners successfully moved the State Court to compel William to arbitrate his claims against Gomendi based upon the preclusive effect of the Federal Court Order. It is just such potential collateral estoppel effects of the federal court proceeding which renders Gomendi an indispensable party to the Federal Action. See, e.g., Takeda v. Northwestern National Life Insurance Company, 765 F.2d 815 (9th Cir. 1985).

arbitration controversies, as espoused by this Court in Moses H. Cone, permit a federal court to adjudicate a portion of an arbitration dispute which a state court is in the process of adjudicating, where the federal court does not have subject matter jurisdiction to resolve the entire arbitration controversy? The Federal Court interpretation of Moses H. Cone conflicts with established precedent [E.g., Nakash v. Marciano, 882 F.2d 1411 (9th Cir. 1989)] which holds that abstention is appropriate in these circumstances.

3. Does the "protect or effectuate its judgments" exception to 28 U.S.C. § 2283 permit a federal court to enjoin a parallel state court proceeding involving the identical issues, where the state court first exercised jurisdiction over those issues? The decision of this Court in Chick Kam Choo v. Exxon Corporation, 486 U.S. 140 (1988) teaches that it does not apply, thus precluding issuance of the injunction granted in this case. The

Federal Court injunction here and other lower federal court precedent [E.g., McGuire, Cornwell & Blakely v. Grider, 765 F.Supp. 1048 (D.Colo. 1991) and Hunt v. Mobil Oil Corporation, 583 F.Supp. 1092 (S.D.N.Y. 1984)] hold to the contrary.

4. Is the Montana Uniform Arbitration Act's requirement that all contracts with an arbitration clause contain a conspicuous warning notice[11] on the front page pre-empted by the Federal Arbitration Act, despite this Court's ruling in Volt Information Sciences, Inc. v. Board of Trustees, 489 U.S. 468 (1989) that state arbitration law procedural provisions are enforceable if they do not interfere with the Federal Arbitration Act's policy of enforcing voluntary agreements to arbitrate? The Federal

[11]Montana Code Annotated § 27-5-114(4) requires contracts containing arbitration clauses to contain a conspicuous warning notice on the front page of the contract. The Federal Arbitration Act contains no similar provision. The Montana provision does not prohibit arbitration, but is simply designed to insure voluntary and knowing agreements to arbitrate.

Court Order held the warning notice requirement was pre-empted, a ruling which will be the death knell of state efforts to insure that contracting parties knowingly and voluntarily enter into arbitration agreements.

5. Finally, are general state law prohibitions against forum selection clauses, and clauses limiting the time period for bringing legal action, pre-empted by the Federal Arbitration Act, when those provisions are contained in an arbitration clause? Montana law[12]

[12]The Arbitration Clause requires all legal proceedings between the parties to be filed in the State of Wisconsin (Snap-On's home office) and limits the time for bringing any action to one year. Both provisions are prohibited by Montana law. Montana Code Annotated § 28-2-708; State ex rel Polaris Industries v. District Court, 695 P.2d 471 (Mont. 1985); Trammel v. Brotherhood of Locomotive Firemen and Enginemen, 253 P.2d 329 (Mont. 1953). The Arbitration Clause also permits Snap-On to seek court relief on its only meaningful claims against William, yet requires William to arbitrate all of his claims against Snap-On. Such unilateral remedies are impermissible under Montana law, which requires mutuality of remedy in order to enforce contractual provisions. Montana Code Annotated §§ 28-2-301, 28-2-303; see Boise Cascade Corporation v. First Security Bank of Anaconda, 600 P.2d 173 (Mont. 1979). Despite these clear violations of Montana law, the Federal Court enforced the Arbitration Clause. In that these Montana laws are of "general application" to all contracts, the Federal Court's order conflicts with the holding in Perry v. Thomas, 482 U.S. 483, 492 (1987).

prohibits both types of clauses in all contracts, yet the Federal Court held that the Arbitration Clause was enforceable. This conflicts with the holding of Perry v. Thomas, 482 U.S. 483 (1987) that state laws of application to contracts generally are applicable to arbitration agreements.

CONCLUSION

This Court will accomplish nothing by reviewing the May 27, 1993 State Court Order. It was not final and is now moot. Moreover, 9 U.S.C. § 3 has no bearing on this case.

However, should this Court decide to review any issues, those dealing with the proper role of the federal courts in adjudicating arbitration issues pending before state courts should be addressed. Additionally, the pre-emptive effect of the Federal Arbitration Act over state laws designed to insure voluntary, even-handed

agreements to arbitrate deserves the attention of this Court.

The Petition should be denied. Alternatively, if it is granted, this Court should exercise jurisdiction over the entire arbitration controversy, as framed in the Federal Action and State Action.

Dated this 11 day of November, 1993.

Respectfully submitted,

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